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## Mechanisms to Minimize Problem Loans

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Non-performing loans (NPLs) in commercial banks pose a major threat to bank stability and profitability. Non-performing loans can be caused by economic downturns, borrower defaults, poor risk assessment, and various other factors. As a result of reduction of problem loans in banks, the financial health of their loan portfolio will serve to preserve the confidence of depositors and investors.

Credit risk in banks creates serious problems for both lenders and borrowers in the modern financial system. This includes financial losses resulting from the borrower's failure to meet its financial obligations. Understanding the multifaceted nature of credit risk is critical to effective risk management in financial institutions. Therefore, it is necessary to study the various causes of credit risk, its complex determinants and consequences and to manage them wisely [2].

In order to minimize the volume of problem loans, banks are required to effectively apply mechanisms for prevention, early intervention, risk management and regulation.



**Figure 1. Mechanisms to minimize problem loans<sup>1</sup>**

<sup>1</sup> Compiled by the author.

Prevention (Prevention). This is done through effective pre-assessment of credit risk, prudent lending practices and diversification of the loan portfolio . One of the main ways to reduce bad loans is to carry out an accurate credit risk assessment process. Banks should comprehensively assess the creditworthiness of potential borrowers, taking into account their financial status, credit history and solvency.

Banks must adhere to prudent lending practices, in particular, the calculation of the loan amount, the coverage ratio, the customer's cash flow and other indicators should be carefully checked. These measures minimize credit risk.

In addition, diversification of the loan portfolio across different sectors, industries and geographic regions helps mitigate risk concentration and reduce the impact of economic downturns specific to the banking sector.

Early intervention (Early Intervention). Timely monitoring and follow-up, by creating a solid system of credit monitoring in banks, allows early detection of problem loans and signs of difficulties in their clients. Early detection enables banks to take effective measures to prevent loans from becoming NPLs.

When borrowers face financial difficulties, banks can offer options to revise loan terms, interest rates and payment schedules, change loan terms, wait and restructure the loan agreement, taking into account the changing circumstances of borrowers. .

In addition, providing borrowers with access to credit counseling services helps them develop strategies to overcome financial difficulties and repay loan payments [3].

3. Risk management (Risk Management). Through an effective risk management policy, banks should develop and implement comprehensive risk management policies that cover all aspects of the credit process, from origination to collection and collection.

Conduct regular stress tests at banks, which help banks assess how their loan portfolios will perform under adverse economic scenarios. This allows banks to identify potential vulnerabilities and develop contingency plans.

Banks must set aside adequate provisions for expected loan losses, which means they must have sufficient capital to cover potential loan losses. This is the appendix to the decision No. 14/5 of June 13, 2015 of the Board of the Central Bank of the Republic of Uzbekistan in the banking system of Uzbekistan "Procedure for the classification of asset quality in commercial banks and the formation and use of reserves to cover possible losses on assets" according to the regulation on "bank assets are classified into "standard", "substandard", "unsatisfactory", "doubtful" and "bad" categories according to their quality, and mandatory compensation intended to cover possible losses on them reserves are formed as a special reserve of 1 percent, 10 percent, 25 percent, 50 percent, and 100 percent, respectively [1].

4. Regulatory compliance. Prudential standards for banks refer to prudential standards established by banking regulators, including capital adequacy requirements, asset quality classification, and provisioning for potential asset losses. must follow instructions and stress test tasks.

Banks should provide regulators with clear and transparent reporting of NPLs and credit quality metrics, which will enable regulators to effectively monitor and address systemic risks.

The central bank and other supervisory bodies play a decisive role in monitoring the risk management system in the lending practices of commercial banks, ensuring that banks follow best practices and maintain financial stability [4].

The strategy for the collection of loan debts allocated by commercial banks to their customers is developed based on a complete analysis of the data collected by the bank's loan debt analysis department.

In conclusion, it can be said that the reduction of problem loans is necessary not only for the

financial health of banks, but also for the overall stability of the financial system. Therefore, it is very important to implement comprehensive mechanisms to solve these problems.

### **List of references**

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